Service Date: October 22, 1993

DEPARTMENT OF PUBLIC SERVICE REGULATION
BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MONTANA

* * * * * * *

IN THE MATTER OF the Application	)	UTILITY DIVISION
of the MONTANA POWER COMPANY for	)	
Authority to Increase Rates for	)	DOCKET NO. 93.6.24
Natural Gas and Electric Service.	)	INTERIM ORDER NO. 5709b

INTERIM ORDER

Introduction

1. The Montana Power Company (MPC or Applicant) filed on June 21, 1993, its application for increased electric and natural gas rates and revenues. The application was assigned Docket Number 93.6.24.

2. MPC requested increased electric annual revenues of $36,198,499, which is an increase of 11.36 percent on an equiproportional basis. For its natural gas utility MPC requested increased annual revenues of $10,264,608, which is an increase of 10.73 percent on an equiproportional basis. Additionally, MPC requested that the Public Service Commission (Commission or PSC) authorize on an interim basis increased annual revenues for its electric utility of $20,966,813, or 6.4 percent, and increased annual revenues for its natural gas utility of $8,119,994, or 8.49 percent. MPC filed a calendar 1992 test period.

3. The Montana Consumer Counsel (MCC) filed its response to MPC's application on September 7, 1993. MCC recommends a decrease of $4,501,754 in MPC's annual electric revenues and an increase of $1,484,704 in annual natural gas revenues.

4. Previously, the Commission has relied on Commission orders and the testimony, exhibits and data responses of the Applicant. Beginning with this Docket, procedural schedules are expedited, allowing the Commission access to information from both the Applicant and interested parties, as well as information from Commission orders. Accordingly, the Commission has computed the interim for the electric and natural gas utilities by using established practices for setting interim rates (see, ARM 38.5.501, et seq.), and also relied on the prefiled testimony, exhibits and data responses of MPC and MCC.

Major Contested Issues Not Included for Interim

5. The Commission finds that the following five major contested issues shall not be included for interim treatment:

	Electric Revenue Requirement	Gas Revenue Requirement
Full Tax Normalization (FAS 109)	$2,885,749	$691,854
Other Post Employment Benefits (FAS 106)	1,513,724	352,263
Power Supply Cost	2,192,870	electric only
Future Use Gas Wells	gas only	334,377
Shelby Storage	gas only	326,630

Year End Rate Base

6. This is the first time that a major utility has requested a year end rate base under the Commission's optional filing rules. The Commission finds the year end rate base proper for calculating interim treatment in this Docket. The Commission makes the year end rate base calculation for interim purposes by using a combination of MPC and MCC prefiled information.

Depreciation Reserve Adjustment

7. The MCC proposes to include an additional year's depreciation, depletion and amortization expense in the 1992 year end reserve balances. The Commission finds that this rate base adjustment be recognized for interim purposes because of Commission precedent. The proposed adjustment reduces the electric utility rate base by $39,938,318 and the gas utility rate base by $8,920,451.

Year End Customer Count

8. MPC filed this case under the optional filing standards. ARM . 38.5.601(1) (e) provides:

> "For matching purposes, test year revenues shall be restated to reflect end of year customer counts...."

Rather than using the actual end of year customer count, MPC "shaped" the end of year customer count based on the actual number of customers at the end of each month in 1983. MCC witness Mr. Clark noted that there is no "shaping" contemplated or required by the optional rule and recommended eliminating the year end customer count "shaping." The Commission finds that Mr. Clark's interpretation of the optional rules is proper for interim purposes. This adjustment decreases the electric revenue requirement by $431,723 and the gas revenue requirement by $737,640.

Cost of Capital

9. MPC requested and the MCC agreed with the following rate of return amounts for the electric utility: Long term debt at 49.37 percent of the capital structure and at a cost of 8.02 percent; preferred stock at 4.64 percent of the capital structure and at a cost of 7.29 percent; and common equity at 45.99 percent of the capital structure. The Commission finds these amounts to be appropriate for interim purposes.

10. MPC requested and the MCC agreed with the following rate of return amounts for the natural gas utility: Long term debt at 49.37 percent of the capital structure and at a cost of 8.56 percent; preferred stock at 4.64 percent of the capital structure and at a cost of 7.29 percent; and common equity at 45.99 percent of the capital structure. The Commission finds these amounts to be appropriate for interim purposes.

11. MPC requested that 12.5 percent be granted in the final Commission order as the cost of common equity capital for its electric and natural gas utilities, and that 12.1 percent be used for interim purposes. The MCC recommends 10.25 percent for both utilities.

12. In computing interims, the PSC mainly has used the common equity return amount approved in that utility's most recent final order. If this practice were used in this Docket, the Commission would use a 12.1 percent common equity return for both the electric and natural gas utilities. However, the Commission has also made adjustments to the cost of common equity for interim purposes. Such instances have arisen when common knowledge suggests that the cost of capital has changed substantially since the last PSC order was issued for the utility which is under review.

13. The 12.1 percent approved for MPC was granted in July, 1991. Commonly

known and available measures of the cost of capital have fallen substantially since that time. For example, the relatively riskless returns on long term U.S. Government securities have fallen from 8.5 percent to 6 percent, a decline of about 30 percent. Home mortgage rates have fallen by a similar amount, as have the returns on common equity granted by other State Commissions.

14. At the time that the Commission granted the 12.1 percent return to MPC, the average of the returns on equity allowed by other State Commissions was about 12.6 percent. During the first half of 1993 the average of equity returns authorized by other state commission was about 11.7 percent. It has further declined materially during the third quarter, and in several instances the allowed returns have pierced the 11 percent mark.

15. The factors mentioned above suggest that the cost of equity capital for the MPC utilities has declined since July, 1991, by at least a full percentage point. Assuming a close correlation between the slope of the decline line for returns on long term U.S. Government securities and the returns allowed by State Commissions, the decline in the cost of equity capital for the MPC utilities would be substantially more than 1 percent.

16. In order to strike a balance between using the most recent common equity return granted to a particular utility and the substantial and commonly acknowledged decline in the cost of capital, the Commission finds reasonable an 11.25 percent equity return for both the MPC utilities. This return approximates the .9 percent decline in authorized returns from other States for the period 1991 through the first half of 1993, when applied to the previously authorized return on equity of 12.1 percent. This approach is conservative and certainly is appropriate for interim purposes. Using a return on equity of 11.25 percent produces an overall cost of capital for the electric utility of 9.47 percent and an overall cost of capital for the natural gas utility of 9.74

percent.

Matching Test Year Sales and Resources

17. According to MCC witness Mr. Clark, MPC used 7,736,108.7 Mwh to determine the net power supply costs in the test year. In contrast MPC used 7,703,938.9 Mwh to determine test year revenues. Thus, the test year revenues at present rates are produced from 32,169.8 fewer Mwh than are the costs of the test year resources. Mr. Clark proposed to adjust test year revenues in order to provide the necessary match between test year sales and resources. The Commission finds this matching to be proper for interim treatment. This adjustment decreases the electric revenue requirement by $1,584,181.

Affiliated Coal Transaction Adjustment

18. Since the last MPC docket (90.6.39) MPC has reorganized Western Energy Company (WECO). The reorganization greatly reduced WECO's rate base which caused the rate of return for WECO to be increased.

19. The treatment of the WECO reorganization is a contested issue in this Docket. MPC states that the methodology used in 90.6.39 would produce a large increase in the captive coal adjustment (from $2,687,336 to $7,047,429). MPC maintains that based on market prices no captive coal adjustment is appropriate in this Docket. MCC recommends reflecting the WECO reorganization and the full effect, $7,047,429, of the captive coal adjustment.

20. The Commission finds that the methodology used for the captive coal adjustment in Docket 90.6.39, without the WECO reorganization, is appropriate for the determination of interim relief. This adjustment increases the electric revenue requirement by $2,687,336.

Non Major Items Used to Develop the Interim

21. The Commission finds that the following items shall be adjusted from MPC's general case numbers to determine the interim increase: Labor Expense, Labor Related Taxes, Corporate Overhead Charges, Year End Employee Count, Out of Period Least Cost Planning Committee Costs (electric only), Nonconsumable Materials and Supplies (electric only), Mission Valley Power Sale (electric only), Association Dues (gas only), and Interest Synchronization. The Commission made the following rate base adjustments: Cash Working Capital, Relocation Reimbursements, and Year End Accumulated Provision for Depreciation. These adjustments decrease the electric revenue requirement by $1,236,851 and the gas revenue requirement by $298,280.

Conclusion

22. Based on the above Findings of Fact, an increase in MPC's annual electric revenues in the amount of $8,825,155 is necessary to earn an overall rate of return of 9.47 percent.

23. Based on the above Findings of Fact, an increase in MPC's annual natural gas revenues in the amount of $4,025,496 is necessary to earn an overall rate of return of 9.74 percent.

24. The Commission finds that the interest rate that should be applied in calculating any refunds that might result from this Interim Order will be calculated at the return on equity level used in this Interim Order of 11.25 percent.

25. The Commission finds that MPC must apply these annual revenue increases to all customer classes on an equal percentage basis. The Commission directs MPC to file compliance

tariffs reflecting the interim increases for the electric and gas utilities.

CONCLUSIONS OF LAW

1. Applicant, Montana Power Company, provides electric and gas service within the State of Montana and as such is a "public utility" within the meaning of . 69-3-101, MCA.

2. The Montana Public Service Commission properly exercises jurisdiction over the MPC's Montana rates and operations pursuant to Title 69, Chapter 3, MCA.

3. Section 69-3-304, MCA, provides that the Commission may, in its discretion, make temporary approvals of requests pending a hearing or final decision.

4. The rate levels and spread approved in this Order are a reasonable means of providing interim relief to MPC. The rebate provisions of . 69-3-304, MCA, protect ratepayers until there is final order in this Docket.

ORDER

THEREFORE THE MONTANA PUBLIC SERVICE COMMISSION ORDERS THAT:

1. Applicant, Montana Power Company, shall implement on an interim basis rates designed to increase annual Montana jurisdictional electric revenues by $8,825,155 (after the REC allocation) on a uniform percentage basis.

2. Applicant, Montana Power Company, shall implement on an interim basis rates designed to increase annual natural gas revenues by $4,025,496 on a uniform percentage basis.

3. Applicant shall adhere to and abide by all Findings of Fact in this Interim Order, and rate schedules shall comport with all Commission determinations set forth in this Interim Order.

4. Applicant must file tariffs in compliance with the Findings of Fact in this Interim

Order.

5. Nothing in this Interim Order precludes the Commission from adopting in its Final Order, after reviewing the entire record in this Docket, a revenue requirement different from that contained in this Interim Order.

6. Any refunds associated with the annual revenue increase granted in this Interim Order will be computed at the level of return on equity approved in this Interim Order of 11.25 percent.

7. Interim approval of any matters in this proceeding should not be viewed as final endorsement by the Commission of any issues, calculations, or methodologies approved in this Interim Order.

8. The interim annual revenue increases granted in this Interim Order are to be effective for service rendered on and after October 18, 1993.

DONE IN OPEN SESSION at Helena, Montana, this 18th day of October, 1993, by a 5 - 0 vote.

BY ORDER OF THE MONTANA PUBLIC SERVICE COMMISSION

BOB ANDERSON, Chairman

BOB ROWE, Vice Chairman

DAVE FISHER, Commissioner

NANCY McCAFFREE, Commissioner

DANNY OBERG, Commissioner

ATTEST:

Kathlene M. Anderson
Commission Secretary

(SEAL)

NOTE: Any interested party may request that the Commission reconsider this decision. A motion to reconsider must be filed within ten (10) days. See 38.2.4806, ARM.